



*4<sup>th</sup> Street Bridge, Los Angeles*

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# Sales and Use Taxes

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## Revenues

California sales and use tax revenue totaled \$38.1 billion in 2003-04, an increase of 6.5 percent from the \$35.7 billion total in 2002-03.

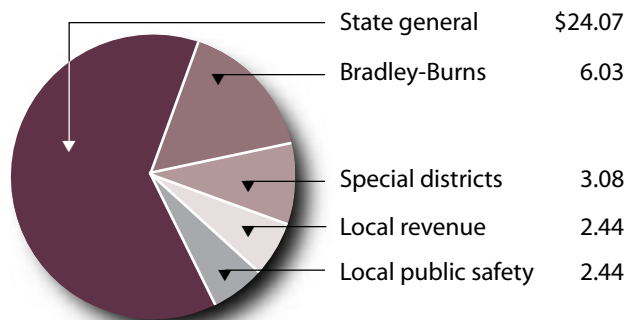
Sales and use tax revenue included:

- \$28.95 billion from the 6.00 percent state sales tax, with
  - \$24.07 billion allocated to the state's General Fund; tax rate of 5.00 percent.
  - \$2.44 billion allocated to the state's Local Revenue Fund; tax rate of 0.50 percent.
  - \$2.44 billion allocated to the Local Public Safety Fund; tax rate of 0.50 percent.
- \$6.03 billion from the 1.25 percent Bradley-Burns Uniform Local Sales and Use Tax, allocated among all of the state's 58 counties and 478 cities.
- \$3.08 billion in special district transactions (sales) and use tax; rates vary by district.

Sales and use tax allocations to the General Fund were 6.4 percent higher than in 2002-03.

### 2003-04 Sales and Use Tax Revenues

Billions of Dollars



Programs

Retailers engaged in business in California pay the state’s sales tax, which applies to all retail sales of goods and merchandise except those sales specifically exempted by law. The use tax generally applies to the storage, use, or other consumption in California of goods purchased from retailers in transactions not subject to the sales tax. Use tax may also apply to purchases shipped to a California consumer from another state, including purchases made by mail order, telephone, or Internet.

The sales and use tax rate in a specific California location has three parts: the state tax rate, the local tax rate, and any district tax rate that may be in effect. The statewide combined sales and local tax rate was 7.25 percent in fiscal year 2003-04 (6.00 percent state tax rate and 1.25 percent local tax rate).

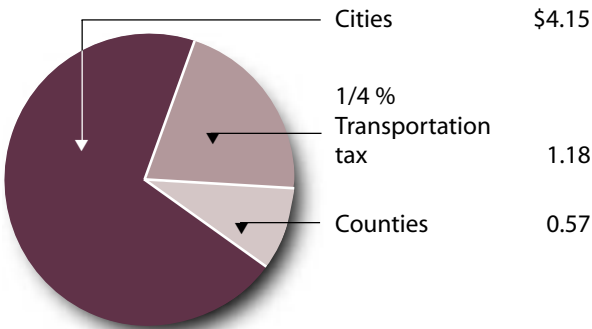
State sales and use taxes provide revenue to the state’s General Fund, to cities and counties through specific state fund allocations, and to other local jurisdictions.

Local Sales and Use Tax

In 2003-04, the Board of Equalization collected and allocated the 1.25 percent Bradley-Burns Uniform Local Sales and Use Tax for all California cities and counties. For each sale, 0.25 percent of the local tax was allocated to the county where negotiations for the sale occurred, for local transportation projects. The remaining 1.00 percent local tax was allocated to the county or an incorporated city, generally depending on the location of the sales negotiations.

Legislation reducing the local tax rate was enacted this fiscal year. For more information, see “Sales and Property Tax Swap,” on [page 30](#).

2003-04 Local Sales and Use Tax Distributions  
Billions of Dollars



City and county local tax distributions are detailed in Table 21A of the Appendix, beginning on page [A-26](#).

**Redevelopment Agencies.** Between 1981 and 1994, cities could finance redevelopment projects with revenue derived from the local sales and use tax and distributed under agreement to city redevelopment agencies. While this authority was repealed effective January 1, 1994, existing city ordinances were permitted to continue. As of June 30, 2004, 33 redevelopment projects in 26 California cities were receiving sales and use tax revenue.

### **District Transactions (Sales) and Use Tax**

The Board of Equalization collects and distributes district transactions (sales) and use tax on behalf of voter-approved district taxes throughout the state. The districts fund a range of local services and infrastructure, including general government, transportation projects, open space, hospitals, and public libraries. Some California locations lie within more than one tax district. A complete list of tax districts, jurisdictions, and revenues is found in Appendix Table 21C, on page [A-30](#).

At the beginning of the 2003-04 fiscal year, there were 40 district taxes in effect, with rates ranging from 0.125 percent to 0.50 percent.

Two additional district taxes went into effect on October 1, 2003, and April 1, 2004, respectively, both with rates of 0.50 percent: the City of Willits and City of Point Arena Transactions and Use Taxes.

Sales made by retailers engaged in business in a jurisdiction levying a district tax are subject to a total sales tax rate that includes the statewide rate and the applicable district tax rate (see Appendix Table 23B, on page [A-33](#)). While the provisions of the Transactions and Use Tax Law are similar to state and local sales and use tax laws, significant differences do exist. These include an exemption for sales shipped to a location outside the district for use in that location and special requirements for sales of aircraft, registered vehicles, and undocumented vessels.

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## **Operations**

The Board encourages voluntary tax law compliance and offers sales and use tax assistance through its Sacramento headquarters and 27 field offices located across the state. Board staff in the agency's New York, Chicago, Houston, and Sacramento Out-of-State field offices assist taxpayers located outside California who are registered to do business in this state.

The number of registered sellers increased this fiscal year, reaching 1,067,374 by June 30, 2004. The agency processed more than 2.9 million sales and use tax returns.

### **Compliance Activities**

Board compliance staff ensure that sellers properly comply with permit requirements, assist them in interpreting tax laws and regulations, provide classroom instruction and individual assistance in the correct preparation of tax returns, and collect outstanding tax amounts. In 2003-04, compliance staff collected more than \$650 million in delinquent sales and use taxes.

### **Consumer Use Tax Section**

The Consumer Use Tax Section works closely with state and federal agencies in administering the use tax due on nondealer sales of vehicles, vessels, aircraft, and mobile homes and on purchases identified on customs declarations. In 2003-04, revenues totaled \$706.7 million, including funds collected by the Board and

- \$598.7 million collected by the Department of Motor Vehicles.
- \$8.5 million collected by the Department of Housing and Community Development.

Consumer use tax revenues this fiscal year increased by 9.9 percent over 2002-03.

### **Audit Program**

The Board maintains an effective audit program to ensure that businesses report neither more nor less tax than required. The program audits nearly 1.3 percent of active master accounts each year, concentrating on those considered most likely to be inaccurate in their tax reporting. In fiscal year 2003-04, the sales and use tax audit program disclosed net deficiencies of more than \$370.7 million. Taxpayers received nearly \$128 million in sales and use tax refunds.

### **Areas of Taxpayer Noncompliance**

As required by the Taxpayers' Bill of Rights, the Board annually

- Identifies the areas of the Sales and Use Tax Law where taxpayer noncompliance is highest.
- Classifies the types of businesses making errors.

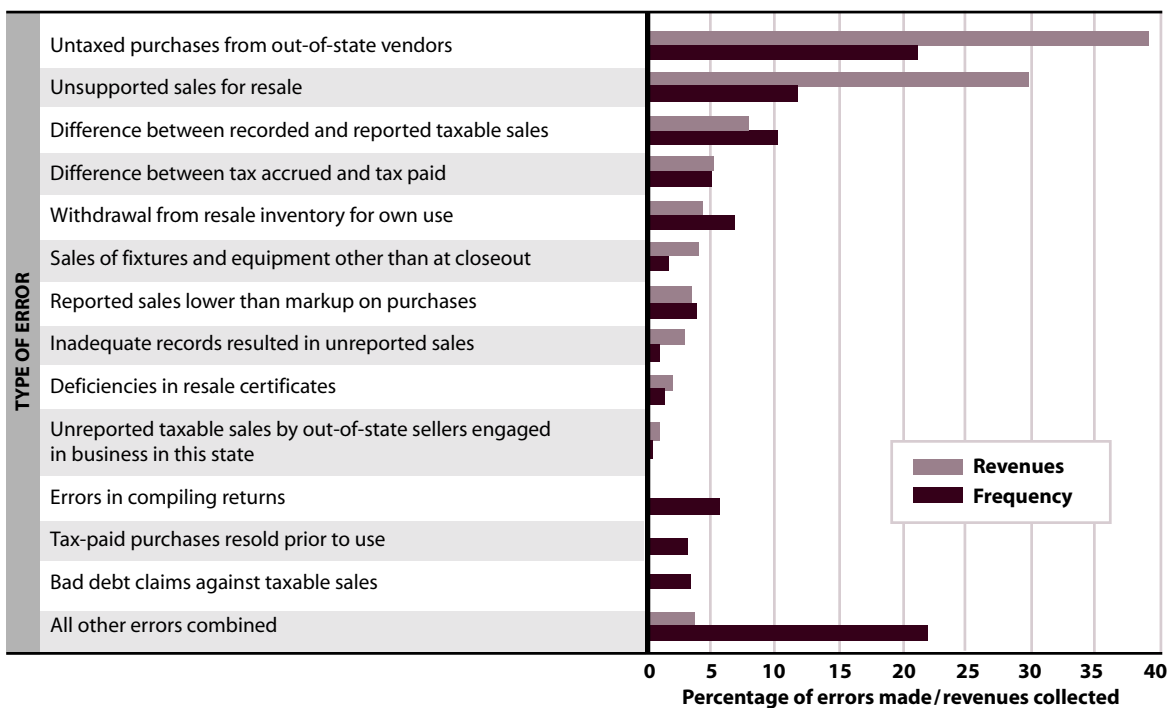
Two categories of taxpayer noncompliance have topped both lists in recent years: failing to pay use tax on purchases from out-of-state vendors and making sales for resale without required documentation. More than one in five taxpayer errors involved unpaid tax on out-of-state purchases. This common error produced more than 38.8 percent of net sales and use tax audit deficiencies (less refunds), totaling more than \$117 million in unpaid tax. More than one in ten taxpayer errors involved an unsupported sale for resale. This noncompliance category accounted

for more than 29.3 percent of all net sales and use tax audit deficiencies (less refunds) or more than \$88 million in unpaid tax.

See below for findings on the types of taxpayer noncompliance for 2003-04 and other tax compliance information required by the Taxpayers' Bill of Rights.

## 2003-04 Analysis of Noncompliance

### Types of Noncompliance Frequency of Errors/Revenues Collected



### Types of Business Making Error Ranked by Revenues Collected

Type of Business	Ranked by Revenues Collected	
	Percentage	Rank for 2002-03
Manufacturers and Wholesalers of Electronic Equipment	24.07	2
Publishers; Producers and Distributors of Light Industrial Equipment	10.44	1
Repair and Hand Trade Shops	6.71	10
Manufacturers and Wholesalers of Store and Office Equipment	5.37	4
Full-Time Specialty Stores	5.28	9
Office Stores and School Furniture Equipment Stores	4.93	5
Business Service Concerns	3.96	20
Used Automobile Dealers	3.81	13
Public Utilities, Transportation, and Allied Services	3.76	3
Construction Contractors and Sellers of Building Materials	3.21	6
All Other Businesses	28.46	
<b>Total</b>	<b>100.00</b>	

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## Appeals

Taxpayers who disagree with Board audit results or other decisions regarding the application of sales or use tax may take advantage of the Board's administrative appeals process. For information on appeals filed in 2003-04, see chapter 6, "Appeals," which begins on [page 47](#).

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## Court Decisions

### Bankruptcy Court Jurisdiction

Under Bankruptcy Code section 505(a)(1), a bankruptcy court has jurisdiction to consider the legality and amount of a taxpayer's sales tax liability when the taxpayer files bankruptcy before the Board of Equalization's final liability determination. Under Bankruptcy Code section 505(a)(2), a bankruptcy court does not have such jurisdiction after a Board redetermination becomes final.

*In re Mantz* (9th Cir. 2003) 343 F.3d 1207

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## Legislation

### Sales and Property Tax Swap (the "Triple Flip")

The original triple flip bills, Assembly Bill 7 and Assembly Bill 1766, enacted the California Fiscal Recovery Act and authorized the state to issue up to \$10.7 billion in bonds to finance the cumulative 2002-03 budget deficit. Assembly Bill 7 increased the state sales tax rate by 0.50 percent and decreased the Bradley-Burns local sales tax rate by the same amount. Assembly Bill 1766 implemented the property tax component of the triple flip, providing a mechanism to allow cities and counties to retain more property tax revenue to compensate them for reduced local sales tax revenue.

*Assembly Bill 7, Chapter 13 of the First Extraordinary Session, Statutes of 2003; Assembly Bill 1766, Chapter 162, Statutes of 2003; superseded by Assembly Bill 9, below.*

Assembly Bill 9 changed the state and local sales tax adjustments proposed under the original triple flip bills to 0.25 percent each, effective July 1, 2004. The bill also enacted the Economic Recovery Bond Act and authorized the issuance of up to \$15 billion of bonds to finance the accumulated budget deficit. The voters approved the bond measure as Proposition 57 on March 2, 2004.

*Assembly Bill 9, Chapter 2 of the Fifth Extraordinary Session, Statutes of 2003; operative July 1, 2004*

### Exemption for Meals and Food—Nonprofit Veterans Organizations

Provides a sales and use tax exemption for sales of meals and food furnished or served by a nonprofit veterans organization to raise funds.

*Assembly Bill 189, Chapter 721, Statutes of 2003; effective April 1, 2004*

**California Domestic Partners**

Provides that under California law, registered domestic partners have the same rights, protections, benefits, responsibilities, obligations, and legal duties as spouses. This is true whether the rights and responsibilities come from statutes, administrative regulations, court rules, government policies, common law, or any other provisions or sources of law, except the California Constitution or a statute adopted by initiative.

*Assembly Bill 205, Chapter 421, Statutes of 2003; effective January 1, 2004, but operative January 1, 2005*

**Agency Consolidation Study**

Requires the Legislative Analyst to submit a report to the Legislature on the consolidation of the remittance processing, cashiering, and mail processing operations of the Board of Equalization, Franchise Tax Board, and Employment Development Department.

*Assembly Bill 986, Chapter 569, Statutes of 2003; effective January 1, 2004*

**Managed Audit Program**

This Board of Equalization-sponsored measure grants the Board the authority to establish a Managed Audit Program. The program would allow taxpayers to perform audits of their own books and records, with limited Board guidance, in return for a 50 percent reduction in the interest rate applicable to any tax liabilities disclosed in the audit.

*Assembly Bill 1043, Chapter 87, Statutes of 2003; effective January 1, 2004*

**Voluntary Use Tax Reporting**

Provides that when a qualified California purchaser voluntarily reports use tax obligations, the purchaser's liability for past-due use tax is limited to the three prior years. Also requires the Board to prepare a report to the Legislature on the benefits of this provision. Expires January 1, 2006.

*Assembly Bill 1741, Chapter 697, Statutes of 2003; effective January 1, 2004*



*Paintersville Bridge, Sacramento River*



**Streamlined Sales Tax Project**

Enacts the “Streamlined Sales Tax Project” to create a state Board of Governance to represent California in meetings related to the Streamlined Sales and Use Tax Agreement, a national effort intended to address sales and use tax issues related to interstate sales.

*Senate Bill 157, Chapter 702, Statutes of 2003; effective January 1, 2004*

**Sale and Leaseback of Public Passenger Transportation Vehicles**

Extends until January 1, 2009, the existing sales and use tax exemption for the sale and leaseback of public passenger transportation vehicles by a transit authority, special district, or governmental entity. The bill also establishes that if the exemption is repealed, no tax is due on the purchase of a covered vehicle by a qualifying party who first leased the vehicle while the exemption was in effect.

*Senate Bill 760, Chapter 597, Statutes of 2003; effective January 1, 2004*

**Bunker Fuel Exemption**

Provides a sales and use tax exemption for the sale of fuel and petroleum products (bunker fuel) to a water common carrier for immediate shipment outside California in ships that will use the fuel outside the state.

*Senate Bill 808, Chapter 712, Statutes of 2003; effective April 1, 2004*

**Use Tax Reporting**

Authorizes California taxpayers to report use tax on their California income tax returns for purchases made from January 1, 2003, through December 31, 2009. This bill also prohibits the state from purchasing goods from vendors that are not registered with the Board, with some exceptions.

*Senate Bill 1009, Chapter 718, Statutes of 2003; effective January 1, 2004*

**City and County Permit Information**

Extends indefinitely the legal provision allowing cities and counties to collect and transmit to the Board information from businesses that will make taxable sales in their jurisdictions.

*Senate Bill 1062, Chapter 471, Statutes of 2003; effective January 1, 2004*



*Humboldt Bay Bridge*

**Manufacturers’  
Income Tax Credit  
Refunds**

Clarifies the circumstances under which a person may claim a refund with the Board of Equalization for the manufacturers’ income tax credit allowed under the state’s Personal Income and Corporation Tax laws.

*Senate Bill 1064, Chapter 606, Statutes of 2003; effective January 1, 2004*

**Transactions  
and Use Taxes****Transactions and Use Tax—County of Los Angeles**

Authorizes the Los Angeles County Metropolitan Transportation Authority, with two-thirds voter approval, to levy a 0.50 percent transactions (sales) and use tax for up to six and one-half years for transportation-related capital projects and programs.

*Senate Bill 314, Chapter 785, Statutes of 2003; effective January 1, 2004*

**District Taxes—Maximum Combined County Rate  
and City Imposition**

Increases from 1.50 percent to 2 percent the maximum combined rate of transactions (sales) and use taxes that may be levied within a county. Authorizes cities to levy district taxes at a rate of 0.25 percent, or multiples of 0.25 percent, for general or special purposes without first seeking special enabling legislation.

*Senate Bill 566, Chapter 709, Statutes of 2003; effective January 1, 2004*

**Transportation Transactions and Use Tax—Time Limit**

Provides that a transactions and use tax imposed for transportation purposes will remain in effect for the period of time designated in the tax ordinance and deletes the previous 20-year time limit in Public Utilities Code section 18021.

*Assembly Bill 427, Chapter 129, Statutes of 2003; effective January 1, 2004*

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**Regulations****Medicines and  
Medical Devices**

Regulation 1591, *Medicines and Medical Devices*, was amended to provide that breast and tissue expanders should be considered prosthetic devices.

*Title 18, California Code of Regulations, section 1591; effective February 25, 2004*

**Eyeglasses and  
Other Ophthalmic  
Materials**

Regulation 1592, *Eyeglasses and Other Ophthalmic Materials*, was amended to clarify that for sales and use tax purposes, clip-on sunglasses are treated in the same manner as eyeglasses, frames, and lenses.

*Title 18, California Code of Regulations, section 1592; effective August 17, 2003*

**Diesel Fuel  
Prepayment  
Exemption**

Regulation 1598.1, *Diesel Fuel Prepayment Exemption*, was adopted to implement the provisions of Senate Bill 1901, which enacted Revenue and Taxation Code section 6480.3. The statute provides an exemption from the sales tax prepayment for certain sales of diesel fuel purchased by a retailer for resale to qualifying farmers or food processors, as defined in Regulation 1533.2, *Diesel Fuel Used in Farming Activities or Food Processing*. The regulation defines terms used in SB 1901, clarifies acceptance criteria for diesel fuel prepayment exemption certificates, provides guidelines on the form of an exemption certificate, clarifies a retailer's liability for tax when the diesel fuel is resold, and explains the penalties for misuse of the exemption certificate.

*Title 18, California Code of Regulations, section 1598.1; effective October 9, 2003*

**Vehicles and  
Trailers for Use  
in Interstate or  
Out-of-State  
Commerce**

Regulation 1620.1, *Sales of Certain Vehicles and Trailers for Use in Interstate or Out-of-State Commerce*, was adopted to provide definitions of key terms used in Revenue and Taxation Code sections 6388 and 6388.5, to address the application of tax to sales of certain vehicles and trailers delivered to purchasers in California, to provide criteria for properly completing an affidavit, to provide guidelines for lessors, and to provide recordkeeping requirements for purchasers of the vehicles and trailers.

*Title 18, California Code of Regulations, section 1620.1; effective October 16, 2003*



*7<sup>th</sup> Street Bridge, Los Angeles*

**Packers, Loaders,  
and Shippers**

Regulation 1630, *Packers, Loaders, and Shippers*, was amended to provide that when a shipper, under contract to a customer, provides a disposable temperature recording device to accompany perishable food products to an out-of-state destination, the shipper's sale of the device is an exempt sale in interstate commerce under Revenue and Taxation Code section 6396.

*Title 18, California Code of Regulations, section 1630; effective October 15, 2003*

**Bradley-Burns  
Uniform Local  
Sales and Use Tax****Place of Sale and Use**

Regulation 1802, *Place of Sale and Use for Purposes of Bradley-Burns Uniform Local Sales and Use Taxes*, was amended to clarify that local sales tax revenue can only be allocated to a retailer's California sales office if that office participates in the sale. It also specifies that if a retailer has more than one California business location, the sale occurs at the place of business that participated in the sale.

*Title 18, California Code of Regulations, section 1802; effective November 28, 2003*

**Motor Vehicle Leases**

Regulation 1803.5, *Long-Term Leases of Motor Vehicles*, was adopted to interpret and explain the allocation of local use tax revenues from long-term leases of motor vehicles.

*Title 18, California Code of Regulations, section 1803.5; effective July 26, 2003*